



**DEPARTMENT OF HEALTH & HUMAN SERVICES**  
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**NOV 9 2004**

Report Number: A-03-04-00213

Patrick W. Finnerty, Director  
Department of Medical Assistance Services  
Commonwealth of Virginia  
600 East Broad Street, Suite 1300  
Richmond, Virginia 23219

Dear Mr. Finnerty:

Enclosed are two copies of the Department of Health and Human Services (HHS), Office of Inspector General (OIG) final report entitled "Review of Virginia's Contingency Fee Payments for Maximizing Federal Revenues Claimed by Its Medicaid Managed Care Program." A copy of this report will be forwarded to the action official noted below for his/her review and any action deemed necessary.

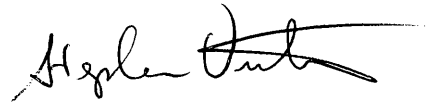
Final determination as to actions taken on all matters reported will be made by the HHS action official named below. We request that you respond to the HHS action official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

In accordance with the principles of the Freedom of Information Act (5 U.S.C. § 552, as amended by Public Law 104-231), OIG reports issued to the department's grantees and contractors are made available to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the department chooses to exercise. (See 45 CFR part 5.)

If you have any questions or comments about this report, please do not hesitate to call me at 215-861-4470 or contact me through e-mail at [stephen.virbitsky@oig.hhs.gov](mailto:stephen.virbitsky@oig.hhs.gov).

Please refer to report number A-03-04-00213 in all correspondence.

Sincerely,

A handwritten signature in black ink, appearing to read "Stephen Virbitsky", with a long horizontal flourish extending to the right.

Stephen Virbitsky  
Regional Inspector General  
for Audit Services

Enclosures - as stated

**Direct Reply to HHS Action Official:**

Nancy B. O'Connor, Acting Regional Administrator  
Centers for Medicare & Medicaid Services  
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Public Ledger Building, Suite 216  
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Philadelphia, Pennsylvania 19106

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF VIRGINIA'S  
CONTINGENCY FEE PAYMENTS FOR  
MAXIMIZING FEDERAL REVENUES  
CLAIMED BY ITS MEDICAID  
MANAGED CARE PROGRAM**



**NOVEMBER 2004  
A-03-04-00213**

# ***Office of Inspector General***

**<http://oig.hhs.gov>**

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The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health and Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

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# *Notices*

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## **THIS REPORT IS AVAILABLE TO THE PUBLIC at <http://oig.hhs.gov>**

In accordance with the principles of the Freedom of Information Act, 5 U.S.C. 552, as amended by Public Law 104-231, Office of Inspector General, Office of Audit Services reports are made available to members of the public to the extent the information is not subject to exemptions in the act. (See 45 CFR Part 5.)

## **OAS FINDINGS AND OPINIONS**

The designation of financial or management practices as questionable or a recommendation for the disallowance of costs incurred or claimed, as well as other conclusions and recommendations in this report, represent the findings and opinions of the HHS/OIG/OAS. Authorized officials of the HHS divisions will make final determination on these matters.



## **EXECUTIVE SUMMARY**

### **BACKGROUND**

In 1965, Congress established Medicaid as a jointly funded State and Federal program that provides medical assistance to low-income people that qualify under title XIX of the Social Security Act (the Act). In the Commonwealth of Virginia, the Department of Medical Assistance Services (Virginia) administers the Medicaid program with Federal oversight from the Centers for Medicare & Medicaid Services (CMS), an agency within the Department of Health and Human Services.

Virginia contracted with a consulting firm to calculate the family planning service costs provided by managed care organizations. Family planning service costs are eligible for 90 percent Federal financial participation (FFP). The FFP in Virginia for most other medical services is approximately 50 percent. Virginia paid the firm a fee contingent on the additional FFP generated by identifying additional expenditures eligible for the 90 percent rate.

Federal guidelines do not allow FFP for fees that are contingent upon recovery of costs from the Federal Government. Contingency fees are allowable if the intent of the contract is to provide Medicaid program savings, not maximize Federal revenue. States receive 50 percent FFP for allowable contingency fee payments and report these payments as a Medicaid administrative cost.

This self-initiated audit resulted from our ongoing audit of Virginia's family planning service costs incurred by its Medicaid managed care program. We will report the results of that audit separately.

### **OBJECTIVE**

The objective of this audit was to determine whether Virginia improperly claimed, as Medicaid administrative costs, contingency fees paid to a consulting firm for Federal revenue maximization services.

### **SUMMARY OF FINDING**

Between October 2001 and April 2003, Virginia claimed \$677,964 in unallowable contingency fee payments made to a consulting firm for providing Federal revenue maximization services. The Federal share of these payments totaled \$338,982. The consulting firm increased Federal revenues for Virginia by identifying expenditures eligible for 90 percent FFP. Virginia stated that it had improperly claimed these fees as Medicaid administrative costs and intended to submit the corrective adjustment.

## **RECOMMENDATION**

We recommend that Virginia refund \$338,982 (\$202,821 for Federal fiscal year 2002 and \$136,161 for Federal fiscal year 2003) for the Federal share of improperly claimed contingency fees of \$677,964.

## **VIRGINIA'S COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE**

Virginia concurred with our finding and recommendation. Virginia agreed to make an adjustment of \$338,982 to refund the Federal share of contingency fee payments it incorrectly claimed as a Medicaid administrative cost. The Office of Inspector General (OIG) is pleased with Virginia's willingness to take corrective action. Virginia's complete comments are found in Appendix A.

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## **INTRODUCTION**

### **BACKGROUND**

#### **Medicaid Overview**

In 1965, Congress established Medicaid as a jointly funded State and Federal program that provides medical assistance to low-income people that qualify under title XIX of the Act. In the Commonwealth of Virginia, the Department of Medical Assistance Services administers the Medicaid program with Federal oversight from CMS, an agency within the Department of Health and Human Services.

#### **Medicaid Reporting Requirements**

The CMS requires States to report their Medicaid expenditures, both medical assistance and administrative, on Form CMS-64, Medicaid Program Expenditures Report. The Federal Government pays its share of medical assistance expenditures according to a formula defined in section 1905(b) of the Act. That share is known as the Federal medical assistance percentage. The Federal payment to States for their medical assistance expenditures is referred to as FFP. Section 1903(a)(7) of the Act provides a 50 percent Federal share for each State's administration of its Medicaid program.

Federal guidelines for claiming professional and consultant services are found in Office of Management and Budget (OMB) Circular A-87<sup>1</sup> which states that "costs of professional and consultant services...are allowable...when reasonable in relation to the services rendered and when not contingent upon recovery of the costs from the Federal Government." The CMS allows States to claim certain professional and consulting payments for third-party liability or collection services as an administrative cost (State Medicaid Manual section 2975.6). The CMS clarified this policy in a letter to its regional administrators (November 7, 2002), stating that CMS would allow FFP for contingency fees if the "intent of the contingency fee contract produced Medicaid program savings, not additional expenditures for FFP."

#### **Family Planning Services**

Under section 1905(a)(4)(c) of the Act, State Medicaid programs are required to provide family planning services to Medicaid beneficiaries. The scope of these services is not established in the statute or by regulation. The CMS provided general guidance in section 4270 of the State Medicaid Manual that states that the purpose of the benefit is "to aid those who voluntarily choose not to risk an initial pregnancy." The CMS also issued "Title XIX Financial Management Review Guide (Number 20): Family Planning Services," that identified the procedure codes for reporting these services. Under section 1903(a)(5) of the Act and 42 CFR § 432.50 and 433.15, States may claim 90 percent FFP for the costs of family planning services.

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<sup>1</sup> OMB Circular A-87, "Cost Principles for State, Local and Indian Tribal Governments (Revised May 4, 1995, As Further Amended August 29, 1997), Attachment B, Section 33(a), Professional Service Costs."

Under managed care delivery systems, States pay a capitation rate to managed care organizations that agree to provide specified health services to Medicaid beneficiaries. Virginia contracted with a consulting firm to develop a methodology to calculate the family planning service costs provided by Virginia's managed care organizations. To claim these costs, Virginia multiplied a rate, known as a factor, by its capitation payments. The factor represented the percentage of family planning service costs to total healthcare costs. Virginia paid the consulting firm, under a contingency fee contract (CFC), a percentage of the additional Federal revenues Virginia realized using the family planning factor developed by the consulting firm.

## **OBJECTIVE, SCOPE, AND METHODOLOGY**

### **Objective**

The objective of this audit was to determine whether Virginia improperly claimed, as Medicaid administrative costs, contingency fees paid to a consulting firm for Federal revenue maximization services.

### **Scope**

Our audit included a limited scope review of \$935,613 in contingency fee payments made by Virginia to one consulting firm between October 2001 and April 2004. According to the contract, the fees paid to the consulting firm were contingent upon the additional Federal revenue recoveries Virginia realized. The recoveries represent the additional FFP Virginia received for claiming 90 percent FFP for the family planning services provided by its Medicaid managed care program.

Our fieldwork was performed at the State agency in Richmond, VA.

### **Methodology**

To accomplish our objective, we:

- Reviewed all relevant criteria including the Act, Federal regulations, OMB Circular A-87, CMS's State Medicaid Manual and policy letters, and Virginia's consulting firm contract.
- Asked Virginia to self-disclose its contingency fee payments and claims of FFP for only those services provided by the consulting firm with respect to family planning services. These fees were reported as part of the State Medicaid administrative expenditures.
- Reviewed Form CMS-64 to confirm an adjustment by Virginia that reversed a previous contingency fee claim for FFP.

We performed our review in accordance with generally accepted government auditing standards. However, our review of internal controls was limited to validating Medicaid administrative costs

claimed by Virginia as contingency fees paid to a consulting firm for Federal revenue maximization services.

## **FINDING AND RECOMMENDATION**

Between October 2001 and April 2003, Virginia claimed \$677,964 in unallowable contingency fee payments made to a consulting firm for providing Federal revenue maximization services. The Federal share of these payments totaled \$338,982. The consulting firm increased Federal revenues for Virginia by identifying expenditures eligible for 90 percent FFP. Virginia stated that it had improperly claimed these fees as a Medicaid administrative cost and intended to submit the corrective adjustment.

### **VIRGINIA IMPROPERLY CLAIMED FEDERAL FINANCIAL PARTICIPATION FOR UNALLOWABLE CONTINGENCY FEE PAYMENTS**

Virginia improperly claimed FFP for \$677,964 in contingency fee payments between October 2001 and April 2003. The Federal share of these payments totaled \$338,982. These claims were reported as a Medicaid administrative cost. Federal guidelines, however, prohibit States to claim FFP for payments that are contingent upon recoveries from the Federal Government. Virginia agreed that it improperly claimed these expenditures. Virginia had adjusted previous improper contingency fee claims but had failed to adjust these claims. Virginia also stated its intention to submit the corrective adjustment.

#### **Federal Guidelines Prohibit FFP for Fees Contingent on Recoveries from the Federal Government**

##### ***OMB Circular A-87: Professional Service Costs***

“Cost of professional and consultant services ...are allowable...when reasonable in relation to the services rendered and when not contingent upon recovery of the costs from the Federal Government.”

##### ***CMS Letter to CMS Regional Administrators: Contingency Fee Payments – Policy Revision***

“The fee must be contingent upon Medicaid cost avoidance savings or recoveries in which the Federal Government shares. The intent of the CFC must be to produce Medicaid program savings, not additional expenditures reported for FFP. Payments contingent upon recoveries from the Federal Government are not allowable.”

#### **Virginia Improperly Claimed FFP for Unallowable Contingency Fee Payments**

Virginia improperly claimed FFP for \$677,964 in contingency fee payments between October 2001 and April 2003. The Federal share of these payments totaled \$338,982. These claims were reported as Medicaid administrative costs. Between October 2001 and April 2004, Virginia paid \$935,613 in contingency fees on the additional FFP generated for identifying the expenditures

eligible for the 90 percent rate. Virginia did not claim FFP for \$257,649 in contingency fees paid between June 2003 and April 2004.

To calculate the expenditures eligible for 90 percent FFP, Virginia multiplied a rate, known as a factor, by its capitation payments. The factor represented the percentage of family planning service costs to total healthcare costs. The following table summarizes the contingency fee payments for family planning services.

**Table 1. Contingency Fee Payments**

<b>Invoice Paid Date</b>	<b>Additional FFP</b>	<b>Contingency Fee</b>	<b>Federal Share Claimed</b>
10/01/2001	\$ 1,309,311	\$ 98,198	\$ 49,099
12/17/2001	1,705,518	127,914	63,957
03/18/2002	1,765,457	105,927	52,964
06/03/2002	1,797,872	73,603	36,801
<b>Federal Fiscal Year 2002</b>	<b>\$ 6,578,158</b>	<b>\$405,642</b>	<b>\$202,821</b>
11/13/2002	\$ 1,411,218	\$ 70,561	\$ 35,280
01/29/2003	2,291,970	114,599	57,299
04/09/2003	1,792,839	87,162	43,581
06/11/2003	1,797,626	80,893	0
<b>Federal Fiscal Year 2003</b>	<b>\$ 7,293,653</b>	<b>\$353,215</b>	<b>\$136,161</b>
01/21/2004	\$ 2,880,978	\$115,559	\$ 0
04/16/2004	1,529,931	61,197	0
<b>Federal Fiscal Year 2004</b>	<b>\$ 4,410,909</b>	<b>\$176,756</b>	<b>\$ 0</b>
<b>Total</b>	<b>\$18,282,720</b>	<b>\$935,613</b>	<b>\$338,982</b>
<b>Contingency Fees Claimed</b>	<b>\$12,074,185</b>	<b>\$677,964</b>	<b>\$338,982</b>
<b>Contingency Fees Unclaimed</b>	<b>\$ 6,208,535</b>	<b>\$257,649</b>	<b>\$ 0</b>

### **Virginia Failed to Adjust Improper Claims**

Virginia agreed that it improperly claimed FFP for these contingency fee payments. It had adjusted a previous improper claim of \$2,037,862<sup>2</sup> (Federal share \$1,018,931) on Form CMS-64 for the quarter ended September 30, 2001. Virginia, however, did not adjust the \$338,982 in FFP claimed for Federal fiscal years 2002 and 2003. Virginia stated its intention to submit a corrective adjustment.

### **Virginia Inflated its Medicaid Administrative Costs**

The Federal share of the improperly claimed contingency fees of \$677,964 totaled \$338,982. These fees improperly inflated Virginia's Medicaid administrative costs.

<sup>2</sup> For these contingency fees, the consulting firm provided family planning as well as non family planning services to maximize Federal reimbursement.

## **RECOMMENDATION**

We recommend that Virginia refund \$338,982 (\$202,821 for Federal fiscal year 2002 and \$136,161 for Federal fiscal year 2003) for the Federal share of improperly claimed contingency fees of \$677,964.

## **VIRGINIA COMMENTS AND OIG RESPONSE**

### **Virginia Comments**

Virginia concurred with our finding and recommendation. Virginia agreed to make an adjustment of \$338,982 to refund the Federal share of contingency fee payments it incorrectly claimed as a Medicaid administrative cost. Virginia's complete comments are found in Appendix A.

### **OIG Response**

The OIG is pleased with Virginia's willingness to take corrective action.

# **APPENDIX**

VIRGINIA COMMENTS



COMMONWEALTH of VIRGINIA  
*Department of Medical Assistance Services*

PATRICK W. FINNERTY  
DIRECTOR

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October 15, 2004

Mr. Stephen Virbitsky  
Regional Inspector General for Audit Services  
Department of Health and Human Services  
Suite 516, The Public Ledger Building  
150 S. Independence Mall, West  
Philadelphia, PA 19106-3499

Dear Mr. Virbitsky:

Report Number A-03-04-00213

Thank you for providing DMAS a copy of the draft report, "Review of Virginia's Contingency Fee Payments for Maximizing Federal Revenues Claimed by Its Medicaid Managed Care Program." DMAS agrees with the validity of the facts and the reasonableness of the recommendation. DMAS will adjust the \$338,982 improperly claimed on Form CMS-64 for the quarter ending September 30, 2004, which is due at the end of October.

If there are any questions, please direct them to William Lessard. He can be reached at (804) 225-4593.

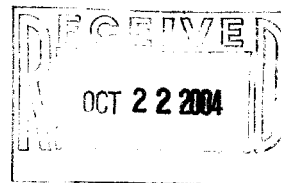
Sincerely,

A handwritten signature in black ink, appearing to read "P. W. Finnerty".

Patrick W. Finnerty

PWF/wjl  
Enclosure

cc. Manju Ganeriwala  
Paul Kirtz  
Scott Crawford  
William Lessard  
Brenda Cooper



## ACKNOWLEDGMENTS

This report was prepared under the direction of Stephen Virbitsky, Regional Inspector General for Audit Services. Other principal Office of Audit Services staff who contributed include:

Robert Baiocco, *Audit Manager*  
David Besterman, *Senior Auditor*  
Lisa Ferraro, *Auditor-in-Charge*  
Kevin King, *Auditor*

For information or copies of this report, please contact the Office of Inspector General's Public Affairs office at (202) 619-1343.